ALPHA + LEONIS
PARTNERS

FROM THE CIO

MARCH, 2022

SPECIAL FOCUS - GEOPOLITICAL RISK FACTORS

Alpha Leonis Partners' CIO reflects on a series of conflicts and massive financial market volatility, and how humanity and the capital markets pushed onward, adjusted, and in the longer run resumed growth and returned to some sense of "normality".

INFLATION AND DEFLATION, REAL CAUSES OF EQUITY VALUE DESTRUCTION

In painful moments of crisis like the one in Ukraine, with human life literally at stake, the headlines suggest prolonged periods of value destruction. History suggests otherwise.

PRIVATE EQUITY DEMONSTRATES ROBUSTNESS

In contrast to public equity, thematic private equity, being inherently less reliant on immediate fiscal and monetary stimuli, appears more robust in times of crisis, and can present compelling opportunities for patient private equity investors.

KYIV WITH DNIEPR RIVER AND PODOLSKY BRIDGE

I am opening this quarter's comments in the face of the continuing war in Ukraine, and accordingly I write with complete solace and respect for the people of Ukraine, who are fighting for their lives. I consciously try to keep politics and emotions out of these writings because the general media errs to the other extreme. But still, at this moment, I had to acknowledge this sentiment before I started my comments because it seems callous and insensitive to write about the capital markets and protecting investor returns. I know that I can speak on behalf of each one of my colleagues within Alpha Leonis Partners, and our client partners, in this respect.

While our duty and professional responsibility are to protect our client capital over the long term, we are also motivated by the fact that our success in generating strong returns fuels greater and greater philanthropic activity across an increasingly broad spectrum of humanitarian causes.

David B. Pinkerton is the CEO and CIO of Alpha Leonis Partners

David brings over 35 years of experience and expertise in focused investment programs in both capital and private markets.

He holds a J.D. degree from Brooklyn Law School and a Bachelor's degree in Finance and Economics from the University of Delaware.

1 TODAY'S CONFLICT WITHIN ITS BIGGER PICTURE CONTEXT

Each time there is a fundamental human crisis like this, and it shakes markets, I have a strong tendency to look back into history when there were other geopolitical conflicts or turmoil at the forefront of investors' minds. This helps to sustain a longer-term perspective during times when current events are emotional, dramatic, and quickly draw investors' attention into the moment. Worst-case or catastrophic thinking preoccupies most media outlets, and hence it is these sets of scenarios that cloud the minds of investors. Sadly, events of geopolitical conflicts, financial turmoil, and now a pandemic are not new to any of us. In my case, revealing my extensive experience, I can call upon having lived through a series of conflicts and massive financial market volatility including:

1986-91	Savings and Loan Crisis
1987	Black Monday
1990s	Various emerging market currency crises
1998	Russian Debt Default, Long Term Capital Management failure
2000	Internet.com bubble burst
2001	September 11 attacks, Afghanistan war, and Enron scandal
2003	Iraq War (2003-2011)
2008	Lehman collapse and Global Financial Crisis
2012	Greek bailout
2014	Crimean invasion
2017	Brexit
2020	Lockdown/Pandemic
2022	Ukrainian/Russian conflict

Even though each one of us would recall and see these past events through different lenses focused and colored by our then-current situations, from my perspective as an observer through the lens of a financial observer, I see that many of these dramatic events were triggered by government actions which is discomforting. Each of us will recall these events and remember them from different perspectives. What it helps to appreciate, especially in the current environment, is to notice that through each one of these recent periods, and even a longer perspective going back 100 years, humanity and the capital markets pushed onward, adjusted, and in the longer run resumed growth and returned to some sense of "normality," even if that benchmark was subsequently altered. Many of the above events have given us a new normal, but peoples and markets have always subsequently prospered.

It may come as a surprise, but geopolitical conflict does not always cause long-term equity value destruction

The current geopolitical conflict is difficult to put into context based upon the recent history, just as was the event that occurred on September 11, 2001. Like then, it is necessary to look back to a longer period of history to see if there are instructive examples of what happened before when there were situations of global conflict that had wider ramifications than just a regional war. Although one could say that the war in Ukraine is another regional conflict, I think that most people will agree that this one has wider geopolitical consequences and is more likely to lead to a protracted period of disruption and adjustment. Without going into the details of how the US equity markets behaved during WWI or WWII, for example as I did in September of 2001, it is fair to summarize that these periods, too, were not long-term destructions of US equity values. It was inflation and a depression in the 1930s that were the more significant contributors to equity value destruction. Sadly, wars themselves often led to war booms in equity markets.

Each time at the moments of maximum crisis, however, headlines reflecting investor sentiment included all the negative fear-provoking words like "recession",

"deleveraging", "job losses", and of course, the more important aspects like the actual loss of human life. Opinions and editorials cite more significant issues such as the state of global democracy, freedom of speech, human rights, sanctions efficacy, climate change, energy policy, and today, bigger picture questions include fears of new reinforced alliances between the other oil-producing nations in the Middle East, and Russia and all these raw material suppliers and their relationship with China. Other topical big picture issues include whether inflation or even stagflation is the new normal, the new implications for global monetary policy and whether the crypto currency movement is reinforced or disabled.

With a few exceptions, adverse events tend to bottom out two to 20 months later

Except for the 1930s, when the depression led to a slow recovery of equity values, and the late 1960s and 1970s when inflation raged consistently for a longer period, what is common to all the aforementioned events is that anywhere from two to 20 months later, significant "bottoms" were formed. After which equity investors were rewarded with exceptionally high returns on capital.

Hence, this time, my focus is to look at the two more "risky" causes of equity value destruction: inflation, and deflation. I believe that, formulating investment strategies in response to these two risks represents a longer-term perspective less skewed by the volatility of daily headlines and grounded in fundamental economic drivers.

2 ADDRESSING INFLATION AND DEFLATION, TWO CAUSES OF EQUITY VALUE DESTRUCTION

First a quick review of how inflation/deflation affects growth and value-oriented equities.

Growth strategies: A rise in long-term rates affects the future valuations of long-duration assets, especially the ultra-long duration themes such as cash flow negative companies. The most visible indication of this is the repricing of the popular ARK Innovation ETF funds, comprised of publicly traded high revenue growth but predominantly loss-making companies. This category of investments (long-dated growth) was most affected in 2021 as interest/discount rates rose and the present value of those future earnings streams declined. Growthy styles are also preferred in deflationary conditions because generally growth is rare, so investors will pay more for the earnings streams of companies that do have growth.

Value strategies: On the other hand, value-oriented equity strategies, tend to be focused on slower revenue-growth companies with pre-existing cash flows/earnings. These are oftentimes, but not always, less affected by rising rates at the long end of the yield curve as they are effectively shorter duration sets of cash flows. These types of investments tend to be more affected by economic cyclicality and perform best when recession risks are receding, and an economic recovery is expected.

To sum up: long duration growth strategies outperform value in deflationary conditions and value-oriented strategies with shorter-duration cash flows, or slow, stable growth, in general outperform when inflation-oriented conditions are present. This is a broad generalization and, of course, each company, industry /or sector, exists on a spectrum of value and growth where investment success is execution, pricing, and value dependent.

So, what are our views on inflationary and/or deflationary risks and how do we construct portfolios to outperform in both potential scenarios?

Outlook for sustained inflation:

The main component of the current spike in inflationary risks is the rapid price increase in fossil fuels and, of course, the post-COVID supply-chain disruption across a variety of industries. Both are predominantly "supply shock" driven and, in our view, not permanent and likely to be adjusted in the intermediate term. Hence, we believe that the inflationary risks are likely to be already "priced in" to assets and are more likely to revert and/trend toward slowing down as opposed to accelerating. This is our base case but of course there are a spectrum of other possibilities that are conditioned upon geopolitical maneuvering and decisions. The risks of politicians making a "mistake" with harmful effects on the world's economy have certainly risen of late.

Four reasons why we think energy prices have more likely than not peaked and are reflecting worst case scenario pricing:

First on oil and gas in general, keep in mind that the supply shock is not because of an absence of oil and gas in terms of proved and probable reserves worldwide. In general, the U.S. has one of the largest supplies of proven reserves, second or third only to Russia; it has just been marginally disabled from production because of regulatory decisions of recent US presidential administration, slower capex increases by shale producers as well as shortage of labor and raw materials needed for oil extraction.

As an additional source of reserve release is that the USA is considering relaxing sanctions with Iran and Venezuela which also could relieve current pressures, but all of these options are constrained by supply-chain challenges of shifting to these new marginal suppliers so this may take some time.

We also recognize that the upcoming election in the US in 2024 will have to be built on avoiding or mitigating inflationary pressures and a key to this will be to onstream as much alternative oil production as possible. Since inflation has the effect of taxing the middle class more than any other segment of the U.S. population, we think that there will be pressure to increase US energy locally in the U.S. and move more towards being energy independent, whether it is carbon, non-carbon derived or clean energy production as well.

Second, the longer-term constraint on inflationary forces is the increasing role that technology has on prices in general. Whether replacing inflation-sensitive human labor in the form of robotics or software, technology **has always been a source of producing better, faster, cheaper** and the USA has one of the best ecosystems for adapting to higher prices via technology applications. Europe also has strength in the technology area especially in countries such as Sweden and Switzerland (two innovation epicenters) who are the top two in the innovation index rankings for 2021.

Third, recall that the current calculations on inflation have been affected by the denominator effect. We all know that there was a significant reduction in the denominator for any percentage calculation because of COVID. As a simple example, if pre-COVID revenues were $100, and then they dropped to $75, and now they are back up to $90, the percentage change today from $75 is 20%, but the percentage change from pre-COVID is minus 10%. This is simple mathematics, but it applies to many recent calculations, whether earnings of a company or percentage changes published on prices of a material.

Finally, inflation is also affected by what might have been overheating conditions of the global economy post-COVID. While we take on a hazard to second guess the U.S. Federal Reserve in its what's to be believed more informed observation of inflation and rates, we think there is more risk to decelerating inflation today than there was 6-9 months ago. We also believe that global GDP growth rates have more risk to the downside than risk to the upside because of the feedback loop to equity valuations and war headlines have on consumer confidence.

Outlook for sustained deflation

Now, as to the risks of a massive, synchronized slowdown in global economies:

I subscribe to the view that most of what caused the Great Depression was a failure of monetary policy to, in effect, provide ample liquidity to the banking system at a time of need and this was a time when monetary policy was not conditioned to be a lender of last resort as it is today. This led to essentially a liquidity crisis that compounded into shrinking demand and supply across an extended period. I believe that the world's central banks have learned this lesson and are much more fearful of massive deflation than of moderate inflation. Over the last 20 years, we have repeatedly seen effective policy responses to thwart liquidity crises by the introduction of Quantative Easing type of approaches. This play book is therefore tested and a ready option, if needed.

We are not to saying that recessions have been abolished or that a prolonged and deep slowdown is out of the question; it is just that we would consider this to be a tail risk and not a base case per se.

The main big picture questions as to this tail risk (i.e., avoiding depression) is whether (or not) the world's central banks, led by the US Federal Reserve, have the debt capacity for more policy stimulus and if one assumes that they do whether (or not) it would be effective anyway. This was a similar concern in every past crisis in the last 20 years and each time there has been an effective stimulus via further government indebtedness.

To get an appreciation for the capacity of a government to exercise continuous quantitative easing one only needs to look at Japan on this point as this government has been implementing repetitive QE longer than any other nation. Japan's debt to GDP ratio has risen to 257% and despite this its currency is still considered a safe haven. The US debt to GDP is much less at approximately 133% and given that the US dollar is a world reserve currency, we think that it has ample room to do more stimulus in an "emergency" situation. Of course, no two countries are the same and many financial economists are divided on this point with the "bears", each time sounding the alarm bells on further QE and the bulls arguing that in the case of the US being the world's creator and empowered holder of a major reserve currency will enable it to command its "exorbitant privilege" of issuing more debt.

To us, all these above macro-economic variables are reinforcing our conviction in our private equity investment strategies. Still, it is of course ignorant to be

blind about what has happened over the last few weeks and assume that private equity will not be affected. If one looks back to WWI and WWII and the great depression as well, the wealth that was preserved over time through these challenging periods was largely through the ownership of privately held and controlled companies, not in government bonds.

In inflationary conditions besides commodities, equities are hands down a better place to retain purchasing power relative to the entire fixed income complex.

For those of you that know us, you will appreciate that at the core our strategy is to invest alongside thematically-focused entrepreneurs in the private markets who emphasize the use of intellectual property to drive high growth and sustainable profitability. We do this in a balanced way to invest across the spectrum of emerging transformers (growth emphasized) to value plays with a growth trigger typically enabled by implementing technology or digitalization on top of a company with established cash flows.

No other business captures the essence and emphasis of our strategy more so than software-based/rich businesses (although this is not the only area where we invest). We believe that growth-based subscription-oriented software models (SaaS) are one of the best places to hide in these types of markets (whether inflation tilted, or deflation tilted) or when traditional input costs are rising, and top-line GDP growth may be threatened. We also think what propelled these themes during COVID (think of Zoom, etc.) are also likely to reinforce to their fundamentals again today. Most software businesses are replacing labor/commodity-intensive inputs and are growing because of this more efficient, and highly profitable scalability. Software-based models are like utilities (read defensive and less cyclical) with often super sticky annual recurring revenues at high margins due to the low marginal costs of licensing that "code".

While cash and bonds, may seem like the near-term hiding places for value preservation, they are likely in the longer-term to face eroding purchasing power due to the potential of rising inflation. In contrast, software models and other IP-driven value propositions that are "game changers" still hold on to their fundamental strengths in earnings growth, whereas most other equities are likely to face challenging earnings headwinds. This does not just apply to SaaS business models, but this also applies to any intellectual property-based asset that is very scalable and innovative in the sense that it is a game-changer versus an incumbent product or service offering.

More broadly speaking, technology, whether it's in robotics, supply chain logistics software, new biopharmaceutical compound discovery, alternative energy and food production, financial service modernization, and many others, has been and will always be, in our opinion, the source of adaptation and evolution that enables adjustments in the global economy. That these changes are often triggered by geopolitical conflicts such as the one we are facing today is unfortunate, but it is the hopeful path forward and the history suggests that humanity and entrepreneurs are consistently able to meet the challenge.

3 CONCLUSION: PUBLIC EQUITY MARKETS FACE MORE DOWNSIDE AS THIS CRISIS IS NOT EASILY CURED BY FISCAL AND MONETARY STIMULI

The current crisis the world is facing may take much longer to recover from because the ramifications are broader and they are not as easily cured by immediate fiscal and monetary stimulus, which enabled quick equity market recovery after the March 2020 nadir of the pandemic. Inflationary forces may persist, (supply-side shocks) and consumer confidence may wane in the face of declining global equity markets. The "buy the dip" savior in the past often was justified by central bank stimulus on the sidelines that existed in the past. Today this "checkbook" may be limited as inflationary forces are curtailing the use of monetary stimulus and furthermore public deficits are containing the normal use of fiscal stimulus.

Accordingly, we are preparing for public equity markets to have potentially more downside from this point forward, driven by the belief that Russia/Putin has his back against the wall to complete its hostile takeover of the Ukraine to prevent its threatening alliances with NATO and a loss of relevance longer term. Russia as a country is in a difficult spot geopolitically because it has a declining population, heavy dependence on commodities and has become globally sanctioned by an increasing number of nations. As I write the Russian government appears to be on the verge of a default on some of its government bonds and this is having contagion risk to other emerging market bond markets and has the potential for widening spreads across the bond market. Fortunately, we have no exposure to spread-oriented (read riskier) government bonds, (no EM) but this is one factor that will affect markets in general.

4 BOTTOM-UP ANALYSIS INDICATES THAT ALPHA LEONIS PARTNERS' PORTFOLIO COMPANIES ARE WELL-POSITIONED TO EXECUTE UPON THEIR STRATEGIES

In addition to always reviewing the top-down risk factors we underwrite all investments to be able to withstand exogenous shocks to the markets and this approach is in essence the foundation upon which we have constructed our knowledge rich, innovation driven investment strategies as this simple component of value creation have been the most persistent and sustainable source of superior investment returns over very long periods of time.

In the bottom-up method of risk analysis, we have analyzed our current exposures in the markets and are confident that the companies we have invested in are well-positioned to continue to execute upon their strategies. A preponderance of them are cash-flow positive and, if not, are well funded to achieve a position of becoming cash-flow positive. With that said there are ramifications on assets in private equity funds that are tied to public market prices and the behavior of the public markets will affect the private markets in the short run.

While we do not rule out the potential for a prolonged recession nor a period where inflation continues, we think that the companies and partners that we have invested with are well-positioned to handle these extreme possibilities under a wide range of scenarios and for the, or more probable set of scenarios, they are also well positioned to prosper over the longer term.

In addition, we believe that, like in past crises, valuations/prices that are currently off their highs (and might have further downside in public markets) will reverse in the longer-term and present compelling opportunities for patient private equity investors.

David B. Pinkerton
Chief Investment Officer

March, 2022
Alpha Leonis Partners AG
Zurich, Switzerland

Contact us for more information:
Alpha Leonis Partners AG
Löwenstrasse 28
CH – 8001 Zürich

contact@alphaleonispartners.com
www.alphaleonispartners.com

LEGAL DISCLAIMER

The content published in this document is provided for general information purposes only. This document is neither an advice on investment nor a recommendation or offer or invitation to make an offer with respect to the purchase or sale of financial instruments. Recipients of this document must not take (or refrain from taking) any investment decision on the basis of the information set out herein. It is not intended to be comprehensive nor to provide any specific legal, tax or other advice and should not be acted or relied upon as doing so. Professional advice appropriate to the specific situation should always be obtained. No information set out, or referred to, in this document shall form the basis of any contract. The information contained herein should not be relied upon by any recipient for any purpose. No securities are being offered by Alpha Leonis Partners AG and Alpha Leonis Partners AG is not soliciting an offer to buy any securities through this document. Any securities that will be offered by Alpha Leonis Partners AG, or any such solicitation, will be made only pursuant to a confidential offering memorandum or similar document and subject to the terms and conditions of definitive documentation (each of which should be read in their entirety) and only in jurisdictions in which such an offer or invitation would be lawful. In particular, this document does not constitute a key information document within the meaning of Art. 58 et seq. of the Swiss Federal Law on Financial Services ("FINSA") or a prospectus within the meaning of Art. 35 et seq. FINSA. This document does not constitute legal, tax, regulatory, accounting or other advice. Certain information contained in this document concerning market and economic trends and overall marketplace opportunities is based on, or derived from, information provided by independent third-party sources. Alpha Leonis Partners AG and/or any of its respective affiliates believes that such information is accurate and that the sources from which it has been obtained are reliable. No representation or warranty is made as to the fairness, accuracy, completeness or correctness of the information contained herein and none of Alpha Leonis Partners AG and/or any of its respective affiliates assumes any responsibility for the accuracy of such information and has not independently verified the accuracy or completeness of such information or the assumptions on which such information is based. Alpha Leonis Partners AG is under no obligation to update, revise or affirm this document following subsequent developments. This document may contain forward-looking statements which involve certain risks and uncertainties. Past performance is not an indication of or guarantee for future results. This document may reflect hypothetical historical performance. This document is not directed at persons subject to legislation that prohibits its distribution or makes its distribution contingent upon an approval. To the maximum extent permitted by law any responsibility or liability of Alpha Leonis Partners AG or of any of its directors, officers or employees is expressly excluded. All disputes arising out of or relating to this document shall be subject to the exclusive jurisdiction of the courts of England and Wales. The contents of this document are protected by copyright. Reproduction, transmission (by electronic or any other means) or modification for public or commercial purposes without the prior written consent of Alpha Leonis Partners AG is prohibited.